DOCUMENT RESUME

ED 086 121 HE 005 029

TITLE	Voluntarism, Tax Reform, and Higher Education.
INSTITUTION	Council for Financial Aid to Education, New York, N.Y.
PUB DATE	Nov 73
NOTE	33p.
AVAILABLE FROM	Council for Financial Aid to Education, 680 Fifth Avenue, New York, New York 10019 ($2.00)
EDRS PRICE	MF-$0.65 HC-$3.29
DESCRIPTORS	*Educational Economics; *Educational Finance; *Financial Support; *Higher Education; *Private Financial Support; School Support

ABSTRACT

Voluntary initiative and voluntary support have been of fundamental importance in the establishment and development of the system of higher education in the U.S. Much of the superior quality of higher education is due to its diversity and its freedom from outside control. Voluntary financial support is one of the vital factors responsible for the independence of educational institutions, public and private alike. Voluntarism is now being challenged through the consideration of several proposals for changing the present tax treatment of private philanthropy. Those who advocate such changes do so in part on grounds of political philosophy and in part on grounds of equity. Some argue that the contributions' deduction encourages taxpayers to spend money that rightfully belongs to the public treasury, and others hold that the benefits of the deduction favor the wealthy vis-a-vis all other taxpayers. Voluntarism should be encouraged. Philanthropy has served as an effective instrument of public policy in channeling private funds to education and has helped to preserve the pluralistic society that is so greatly valued in the U.S. It is imperative that voluntary support should continue to be encouraged by public policy, and that the provisions of the tax incentives should be maintained and strengthened. (Author/PG)

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VOLUNTARISM, TAX REFORM, AND HIGHER EDUCATION

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COUNCIL FOR FINANCIAL AID TO EDUCATION

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VOLUNTARISM, TAX REFORM, AND HIGHER EDUCATION

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November 1973

Prepared by the
Division of Research

Single copies, prepaid, at $2.00. Prices for bulk orders on request.

COUNCIL FOR FINANCIAL AID TO EDUCATION
680 Fifth Avenue, New York, N.Y. 10019

Synopsis

The voluntary contribution of time, effort, and money is one of the hallmarks of American society. This concept, which stands in opposition to an exclusive reliance on government for the achievement of social goals, has been vital in the establishment and preservation of many treasured American institutions.

In particular, voluntary initiative and voluntary support have been of fundamental importance in the establishment and development of the system of higher education in the United States. Much of the superior quality of higher education is due to its diversity and its freedom from outside control. Voluntary financial support is one of the vital factors responsible for the independence of educational institutions, public and private alike.

However, voluntarism is now being challenged through the consideration of several proposals for changing the present tax treatment of private philanthropy. Those who advocate such changes do so in part on grounds of political philosophy and in part on grounds of equity. Some argue that the contributions deduction encourages taxpayers to spend money that rightfully belongs to the public treasury, and others hold that the "benefits" of the deduction favor the wealthy vis-a-vis all other taxpayers.

The first of these views is contrary to the fundamental beliefs which gave rise to the system of voluntary action for the public good; the second argument reflects a misinterpretation of the operation of the tax incentives for educational and charitable contributions and a lack of understanding of who it is that benefits from such voluntary giving.

Among the proposals for altering the tax treatment of charitable gifts are:

1. a reduction in the contribution deduction for gifts of appreciated property,
2. a limitation on the estate tax charitable deduction,
3. a minimum income tax that effectively reduces the maximum contributions deduction (and in some cases eliminates it entirely) for certain high-income taxpayers.

Although these proposals are advanced in the name of greater tax equity, their principal effect would be not to enhance tax equity but to reduce the flow of voluntary philanthropy.

The importance of tax incentives in the growth of voluntary support of higher education is indicated by the historical record. Private gifts and grants to colleges and universities increased from $23 million in 1909-10 to more than $2 billion in 1971-72. The initial upsurge in educational philanthropy prior to 1929-30 coincided with the adoption of the income tax and the charitable contributions deduction, and the extraordinary growth since 1939-40 has taken place against a background of relatively high tax rates.

Since 1965-66 the rate of growth of voluntary support has been only about half the prior postwar level. The upward push on institutional costs from inflation and growing enrollment has been greater in the last six years than previously; this in combination with a slowing of income growth has produced a widespread financial crisis among colleges and universities. The proposals for tax reform, therefore,

would be seriously damaging to higher education since the need now is for more private support, not less.

Voluntarism should be encouraged, not discouraged. Philanthropy has served as an effective instrument of public policy in channelling private funds to education and other desirable areas, and it has helped to preserve the pluralistic society that is so greatly valued in the United States. Any decrease in the tax incentives for charitable giving will lead to reduced private support of the institutions of higher education, thus endangering their solvency and their capacity to serve society. The substitution of additional government appropriations for philanthropic support is both unlikely and undesirable. Reliance on public funding for a disproportionate share of academic income would weaken the values inherent in diversity, jeopardize the freedom and independence of the institutions of higher education, and attenuate the quality and effectiveness of educational programs.

The achievements of higher education in contributing to the progress and welfare of American society have been made possible in large part by the voluntary initiatives of countless individuals who have given their money to support the colleges of their choice. It is imperative that voluntary support should continue to be encouraged by public policy, and that the provisions of the Internal Revenue Code which provide tax incentives for such support should be maintained and strengthened.

I. The Challenge to Voluntarism Summarized

One of the characteristics of American society that has so clearly distinguished it from other societies is its reliance on individual initiative and voluntary action in the achievement of national goals. Unlike the autocratic societies of the past and the collective societies of the present, in which a central authority makes all the decisions that relate to ends and means, American society has held fast to the notion that it is the aggregate of its citizens, functioning individually and cooperatively, that determine objectives and the appropriate ways for reaching them. This characteristic, the propensity for voluntary responsibility and voluntary action, has never quite been matched by any other society in modern times.

Voluntary responsibility and voluntary action inevitably include the practice of free-will giving to charitable endeavors in response to perceived need. *Voluntarism* in this sense has become a basic part of American heritage and the American system of free enterprise, and like that heritage and that system it is uniquely American. In no other country has voluntarism taken root and flourished as it has in the United States; in no other country has private philanthropy for the public good become such a vital part of the national culture and such a deeply-ingrained custom as it has in the United States.

As with other elements of culture and other customs, there is a tendency to take voluntarism for granted and to forget the fact that it has been at the foundation of many of the country's most important and valued institutions. Voluntarism has been responsible for the creation and maintenance of churches, schools, colleges, hospitals, libraries, museums, and the performing arts; voluntarism has given rise to the private health and welfare systems and many other functions and services that are now such an integral part of American civilization and culture.

Tax Reform and Charitable Gifts

Despite its obvious contributions to this country's growth and greatness, this unique system of voluntarism is now being challenged through several proposals for "tax reform" which would fundamentally alter the tax treatment of charitable gifts and contributions. These proposals would, in effect, penalize those who voluntarily support education and other philanthropic activities. As Dr. Jonas Salk, of polio vaccine fame, stated recently in testimony before the House Ways and Means Committee,

> *"... I come before you ... as a scientist who has been enabled through the American system of private philanthropy to carry out his work in a manner that would not have been possible had this system not existed. A rather paradoxical situation is developing in which the system that has been responsible for the success of this country in the war against disease is in the process of being weakened and destroyed." ... "The paradox to which I refer is the contemplation of legislation to reduce incentive* [for private giving] *at a time when Federal funding ... is being diminished."*

Voluntarism, as a part of the American free enterprise system, now involves in one way or another the wealth, the interest, and the personal service of over 70

million people. Although it developed long before the Federal income, gift, and estate taxes came into being, it has for more than a half a century been stimulated and encouraged by those provisions of the tax laws which explicitly recognize that the donor makes a personal sacrifice and contributes to the general welfare when he provides financial support to the philanthropy of his choice. In enacting these provisions, the Congress took into account the incentive effects on voluntary giving and endorsed the view that the citizen has an obligation to support charitable, religious, and educational causes. As they are now written, the tax laws do not bestow any financial benefits on the donors of voluntary funds, rather they eliminate some of the penalties which would otherwise bear on philanthropically-minded taxpayers.

As Norman A. Sugarman, a private attorney and former official of the Internal Revenue Service, said in his testimony to the House Ways and Means Committee on behalf of the Council of Jewish Federations and Welfare Funds, "Charity is not a loophole. Charitable contributions are voluntary and discretionary, and should not be lumped with other deductions with which they have no relationship in regard to character or policy." "The need exists," he continued, "for greater participation, at all levels, in the support of voluntary philanthropy. The tax laws should encourage all people to meet this need rather than discourage their support of voluntary philanthropy."

The Basis for the Challenge

The attack on voluntarism comes from a number of sources, the most important of which are those who object to the tax treatment of philanthropy on grounds of political philosophy. They view the tax savings involved in the contributions deduction as an expenditure of what would otherwise be public revenue, without the appropriate legislative debate and administrative control. Under the existing law, it is said, the taxpayers may spend funds that rightly belong to the public treasury, and this enables individuals and corporations to direct the use of "public" funds according to their own inclinations, preferences, or whims, and often in ways that are inconsistent with national priorities. As such, this argument reflects the belief that all functions and services that are in some sense "public" should be carried out by government, a view that runs counter to the fundamental philosophy which gave rise to and fostered the concept of voluntarism.

There are others who have attacked voluntarism indirectly, and often unintentionally, in the mistaken belief that a taxpayer derives some financial benefit from the provisions which encourage philanthropic giving, and that the size of the benefit is greater for wealthy persons than it is for those in the middle and lower income brackets. This view reflects the notion that while it is equitable to tax increasing incomes at increasing rates, it is somehow inequitable to allow a commensurate tax reduction for that part of income given to charity.

Some are simply unaware or unconvinced of the vast and irreversible changes to American culture and living patterns that would occur if the traditions of voluntarism were to be weakened or eliminated. Others, in their zeal for additional Federal and state funding for vital programs, have lost sight of the crucially important role of private giving in the maintenance of a free society. Whatever the views of those who actively seek to change the tax treatment of philanthropic giving, or of

those who would passively allow such changes to occur, the net result of these tax proposals, if enacted, would be catastrophic for American social organization and life. The voluntary society as it is known today might well disappear. In its place would arise an expansion in the power and responsibility of government, an increasing centralization of authority, and a further enlargement of bureaucratic control over many elements of social activity.

It is clear that changes in the tax laws affecting the incentives for voluntary giving would have an impact far beyond the flow of philanthropic funds between individuals and corporations on the one hand and the legion of voluntary agencies, organizations, and institutions on the other. Although total giving in 1972 is estimated to have exceeded $22 billion, of which $2.02 billion went to higher education, these figures represent only the contributions of money and property. Great numbers of people, 70 million or more, give of their energy and time, as well as their money, on behalf of human needs. Volunteer service is often inspired by and tied to the financial support provided by individual and corporate donors. The dollar value of these volunteer services is incalculable. It follows, therefore, that the discouragement of charitable contributions could have a chilling effect upon all aspects of voluntarism.

The Congress has, for more than 50 years, provided a succession of new provisions in the tax laws aimed at giving further encouragement to private philanthropy for the public good. The Administration has endorsed the view that these provisions should not now be replaced by deterrents to voluntary giving. In a statement presented to the House Ways and Means Committee on April 30, 1973, George P. Schultz, Secretary of the Treasury, said:

> *"We urge that you do nothing which will jeopardize the vitality of our voluntary charities, which depend heavily on gifts and bequests. These organizations are an important influence for diversity and a bulwark against over-reliance on big government. The tax privileges extended to these institutions were purged of abuse in 1969, and we believe the existing deductions for charitable gifts and bequests are an appropriate way to encourage these institutions. We believe the public accepts them as fair."*

Voluntarism and Higher Education

Although voluntarism impinges upon nearly every field of human endeavor, it has been, and is, particularly applicable and especially important to higher education. Voluntary action was chiefly responsible for the establishment of almost all American colleges and universities until the Civil War. In the last hundred years voluntary action and voluntary support preserved, maintained, and strengthened both private and public institutions of higher education. And voluntary financial support currently provides a vital part of the critical resources that are needed by all colleges and universities in the United States. This source of funds has been a major factor in the development of American higher education and in elevating it to a position of excellence.

The Committee for Economic Development, in a recent policy statement,[1]

[1] *The Management and Financing of Colleges*, New York, N.Y., October 1973.

noted that ". . . the flow of private support is essential to the diversity, strength, and vitality of the nation's colleges and universities. It provides a means of achieving the high degree of independence and freedom indispensable to the attainment and preservation of superior quality in education. We therefore conclude that the encouragement of private support is very much in the national interest." The statement concluded with the following recommendation: "We urge that the existing tax incentives for voluntary support of higher education be maintained and, to the extent not incompatible with other objectives, expanded in order to strengthen the base of financial support of all colleges and universities."

In view of the historical relationship between voluntarism and higher education, and because of the importance of voluntary support to colleges and universities and their students, the current proposals for revising the provisions of the tax laws that affect the contributions deduction are potentially of far-reaching consequence to higher education and to American society.

II. How Proposed Tax Reform Threatens Voluntarism, Particularly with Respect to Higher Education

It is clear that the long-standing public policy of encouraging private philanthropy through tax incentives is now being seriously questioned, and that some of the provisions of the tax laws which give expression to this policy are in danger of being modified or eliminated. Many proposals have been put forth for changing the provisions of the present law regarding the tax treatment of charitable gifts, and some of these proposals have been embodied in proposed legislation. These developments merit close scrutiny.

Tax Complexity and Equity

The history of the Internal Revenue Code is one of increasing complexity. The Act of 1954, as amended to include 1972 legislation, is a ponderous document. Its provisions deal with income taxes, employment taxes, estate and gift taxes, excise taxes, and many questions of administration and procedure. Scattered throughout the Code are innumerable definitions and cross-references, the principal purpose of which is to make the law as precise as possible in the context of the complexities of modern economic life. As written, the Code is now so long and complicated that it is doubtful whether any one human being could comprehend it fully.

The increase in the complexity of the Code reflects the social, political, and economic changes that have taken place since the Sixteenth Amendment was adopted in 1913. The income tax itself was initially adopted as a means of securing an adequate revenue for the Federal government, and it reflected a widely-held belief that "income" was an appropriate measure of the taxpayer's ability to pay. The approach to income taxation, however, recognized that the tax should not be applied to gross income, but to some concept of taxable income which allows for certain exclusions and deductions. As time passed, the definition of income itself became increasingly complex, and the exclusions and deductions were re-defined and enlarged in order to provide fully for the special circumstances affecting various groups of taxpayers. Many other provisions were added to implement particular public policies that had nothing whatever to do with taxation as a means of obtaining revenue.

A disproportionate part of the complexity of the Code is contained in the legislation that was enacted after 1939, the reason being that tax rates, which had been relatively low, were sharply increased during the early forties. The continuation of relatively high rates in the post-war years generated urgent concerns with the question of tax equity. Taxpayers' incentives to minimize their taxes also gave rise to numerous tax avoidance arrangements, many of which became the subjects of tax revision because of the undesirable features involved and the amounts of income that were escaping taxation.

Tax Simplification and Reform

The increase in the complexity of the Code and the proliferation of special provisions ultimately generated interest in tax simplification and tax reform. In the late sixties, for example, it became known that a number of high-income persons had so arranged their affairs that they paid little or no tax; in some cases this resulted from the fact that the income was derived from tax-exempt sources, in other cases the taxpayers had qualified for the unlimited charitable deduction and had made sufficient contributions that no taxable income remained, and in yet other cases other special provisions of the tax law were involved. In addition, many specialists in tax law and tax policy recommended simplifying and restructuring many of the complex provisions of the Code.

Public interest in an overhaul of the tax structure, and the concerns of legislators with respect to the questions of tax abuse, tax complexity, and tax equity, ultimately led to a major effort at tax reform in 1969. Even though the Tax Reform Act of 1969 did make a number of significant changes in some of the key provisions of the Code, it did not materially revise the structure of the law. Indeed, it made the law even more complex through the addition of special provisions relating to private foundations and the creation of new forms of preferential income subject to differential tax treatment. Interest in the question of tax reform did not diminish as a result of this Act; on the contrary, tax critics advocated even more strongly the need for a thorough overhaul of the entire tax system.

The Views of the Tax Critics

In its broadest form, the attack on the charitable contributions deduction and other provisions of the Code is part of a general objection to the use of tax incentives to implement various elements of public policy. The argument is that all the special exemptions, deductions, and tax credits, including the provisions relating to charitable giving, are really nothing more than government subsidies of certain activities which are determined outside the normal appropriations process. Some $60 billion in such "tax expenditures" were identified in fiscal year 1971, including $3.75 billion due to the deductibility of charitable contributions.

In weighing tax expenditures versus direct budget appropriations, the tax critics contend, among other things, that tax incentives permit windfalls by paying taxpayers for doing what they would do anyway, and that tax incentives are inequitable in that they are worth more to the high-income taxpayer than the low-income taxpayer. These objections have become most appealing, and the charitable contributions deduction has been attacked principally on these grounds.

Most of the tax critics regard the special income exclusions, the preferential forms of income, and the personal deductions as "loopholes" through which some persons manage to avoid paying their "fair share" of taxes. In this context, the charitable contributions deduction, and particularly the provisions regarding gifts of appreciated property, is typically attacked as a "loophole" on the grounds that the deduction bestows an economic benefit on high-income taxpayers that exceeds the benefit available to low-income taxpayers. They would advocate, as an alternative, either a system of Federal matching grants in which the amount of the matching

payment would be independent of the taxpayer's tax rate, or a system of tax credits in which the amount of the credit would be equal for all taxpayers.

The arguments advanced by the tax reformers rest on a premise that does not accord with the traditional political philosophy of American society. They view any exclusion from income taxation, and particularly the personal deduction for charitable gifts, as though it were a largesse bestowed on the taxpayer by the government for doing something that is largely a matter of personal choice. They argue that this "special favor" is unwarranted as a matter of propriety and equity. They view philanthropic gifts as a form of discretionary spending, like other personal consumption outlays, to be made out of income remaining after taxes. On this interpretation, no taxpayer should have the privilege of making a charitable gift, tax-free.

That this view is contrary to the traditional American concept, which holds that a person should not be taxed on that part of his income given for philanthropic purposes, is amply demonstrated by the continuity of past legislation reaffirming and expanding the tax incentive for charitable giving.

Tax Reform Proposals in 1972

Congressional interest in tax reform beyond the 1969 Act has been evidenced repeatedly since late 1971. The tax reform issue reached a peak during the 1972 elections; the platforms of both major political parties contained strong statements favoring tax equity and tax simplification. Many candidates took positive positions on the tax reform issue as a matter of high priority, and have since urged many specific revisions in the Code. Some of the proposals affecting the charitable contributions deduction are identical to those considered and rejected during the debates on the Tax Reform Act of 1969.

The character of the concern in the Congress over the question of tax reform is illustrated by some of the bills introduced during 1972. No action was taken on any of these bills by the 92nd Congress, and indeed many of them appear to have been "trial balloons" to test the determination of those who advocated sweeping tax reforms. However, they serve to indicate the character of the revisions that could conceivably emerge in 1974.

The *Mills-Mansfield Bill*[2] grouped 54 tax preference provisions, including the charitable contributions deduction, into three classes for outright repeal over a three-year period. It would then have been necessary for the Congress to re-enact them, with or without modification, or to let them remain repealed. The pupose of this action was to force a complete legislative review of these provisions in a systematic and orderly manner.

The *Ullman Bill*[3] would have required the Ways and Means Committee to review these same 54 items, half during 1973 and half during 1974, and to recommend new legislation modifying or repealing them as its study might indicate.

The *Nelson Bill*[4] was much more specific in its suggestions for tax reform. In addition to many other provisions, it would have reduced the deduction for chari-

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[2] The Tax Policy Review Bill, HR 15230, sponsored jointly by Rep. Wilbur Mills (D-Ark.), chairman of the House Ways and Means Committee, and Senate Majority Leader Mike Mansfield (D-Mont.).

[3] HR 15360, sponsored by Rep. Al Ullman (D-Ore.) member of the House Ways and Means Committee.

[4] The Tax Reform Act of 1972, S 3378, sponsored by Sen. Gaylord Nelson (D.Wis.) and 11 other prominent Democratic senators. A companion bill was introduced in the House by Rep. Henry S. Reuss (D.Wis.) and co-sponsored by 24 representatives.

table gifts of long-term appreciated property by one-half the appreciation, made the allowable deduction for such gifts a part of tax preference income, and limited the estate tax charitable deduction to 50% of the adjusted gross estate.

The *Corman Bill*[5] contained most of the specific reform measures proposed in the Nelson Bill, and in addition contained the 3% "threshold" provision; that is, charitable deductions would be allowed only to the extent that they exceed 3% of adjusted gross income. Also, charitable bequests to or for the use of agencies outside the United States would no longer be deductible for estate tax purposes.

Other proposals for tax reform would have had an indirect impact on the operation of the contributions deduction. One such proposal would have put a limit on the total of items designated as "tax preferences." To the extent that any part of charitable contributions, such as gifts of appreciated property, might be so designated, then the limitation would have the effect of reducing the tax incentive for charitable giving in those cases where taxpayers had large amounts of other tax preference income. Another proposal would have taxed the unrealized appreciation on any capital gain property at the time of death, thus reducing the size of many estates which are destined in whole, or as residual bequests, to charitable recipients.

It is clear that these proposals, if enacted, would have a negative effect on philanthropic giving. Indeed, the uncertainty with regard to the future of the contributions deduction itself, which arose as a result of some of the proposed legislation, did have a damaging effect because of doubt as to the continued existence of the five-year carryover provision.

Congressional Interest in Tax Reform in 1973-74

Although no action was taken on any of the bills which surfaced in the Congress in 1972, the question of tax reform and tax simplification carried over the year-end as a legislative issue of high priority. Some of the changes embodied in the 1972 proposals were reintroduced early in the first session of the 93rd Congress, and many Congressmen continued to be highly vocal in their insistence on far-reaching changes in the existing law. As it had previously announced, the House Ways and Means Committee held public hearings on the subject of tax reform during the spring of 1973. Although these hearings encompassed all areas of the Internal Revenue Code, the Committee expressed particular interest in 20 major subjects, including estate and gift tax revision (". . . changes in the unlimited charitable deduction . . .") and the income tax treatment of foundations and charitable contributions.

The Ways and Means Committee has since turned its attention to other subjects. However, it seems clear that it will return to the question of tax reform early in 1974 and that there will be some changes in the tax laws before the Congressional elections in the fall of 1974. It is possible that the proposals for change will receive a more thorough airing than has been usual for tax legislation, because the "closed rule", under which no amendments are permitted to tax bills on the floor of the House, may be relaxed for the first time in many years. The debate on tax reform, therefore, may be very much in the public eye.

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[5] HR 11058, HR 11862, and HR 11863, introduced by Rep. James C. Corman (D.-Calif.), member of the House Ways and Means Committee, and co-sponsored by 25 representatives.

During the course of the hearings on tax reform, in April, 1973, the existing provisions of the law with respect to philanthropic giving were defended vigorously by many eminent persons speaking on behalf of the voluntary sector. In the light of previous indications of Congressional interest, the greatest emphasis was given to proposed changes in the income tax treatment of gifts of appreciated property and the estate tax treatment of charitable bequests. Both of these subjects merit close examination, in part because they have been singled out by tax critics as provisions for which reform is most urgent and necessary, and in part because they affect such a large part of the flow of voluntary support to the institutions of higher education.

Gifts of Appreciated Property

Under the present law, a taxpayer may make a charitable gift in the form of property other than cash. If the property is a capital asset (other than inventory) that the taxpayer has held for more than six months, then he may claim the fair market value of the gift for his contributions deduction, even if the property has a fair market value in excess of its cost (or other tax "basis"). This is a typical situation in instances where charitable gifts of a substantial size are involved. And such gifts, although small in number, represent a very significant share of the total amount of individual giving, particularly in support of higher education, as will be shown below.

According to the critics, the tax treatment of gifts of appreciated property to charity constitutes a particularly egregious inequity in the tax law. The alleged inequity arises from the belief that the taxpayers who have appreciated property, and who are thus in a position to take advantage of this option, are those in the top income brackets. These individuals, it is said, not only get the "benefit" of a reduction in taxes on their ordinary incomes, which is taxed at the highest end of the rate structure, they also avoid paying taxes on the capital gains which would have been due if they had sold their properties instead of given them to charity. Further, it is claimed that in practice such gifts typically involve property for which the tax basis (or cost) is very low, perhaps even zero, and that in such cases it is possible "to make money by giving it away."

The question is a matter of fundamental importance to the entire voluntary sector and especially to higher education. There are really two separate issues involved, (1) whether the argument of the tax critics is technically valid, and if so under what conditions, and (2) whether the provisions of the present law serve the public interest to such an extent as to outweigh the revenue "loss" to the Treasury and other similar considerations.

It is probably true that most charitable gifts in the form of appreciated property are made by taxpayers in the upper brackets. It does not follow, however, that the law discriminates against the lower income taxpayers or that it is in any other way inequitable. Although charitable gifts do reduce the taxes paid by donors, there is no financial gain to the individual taxpayers as a result; rather, there is typically a reduction in the donors' wealth that is larger than their tax "savings." This excess, as well as the tax savings proper, accrues to the benefit of charitable donees. In

short, the diversion of tax revenues from the Treasury goes not to the taxpayers but to philanthropy, and hence to the public good.

The purpose of this provision of the Code is simply to encourage voluntary giving in the public interest, and this particular tax incentive is responsible for a very large portion of gifts by individuals to higher education and other charitable recipients. Since the benefits of voluntary giving accrue to the charitable and educational institutions rather than to the taxpayers who make the gifts, there can be no economic discrimination or inequity in favor of the wealthy in this arrangement.[6]

The assertion that it is possible to make money by giving it away depends upon a specific assumption about the taxpayers' alternatives. The tax critics take the position that wealthy persons typically must sell long-term capital gain property in order to raise the cash they need to pay the taxes due on their ordinary income. Using a hypothetical case in which such property has a zero basis, and in which the taxpayer's tax rates are at a maximum, it is then shown that by giving the property to charity the total Federal tax "savings" can exceed the fair market value of the property itself by about 5%.

While such cases may conceivably exist, the extreme technical requirements would make them very rare. Furthermore, it is highly questionable whether individual taxpayers must make a choice only between the sale or the gift of their property. High income taxpayers typically do not use appreciated assets to pay the taxes due on ordinary income, so they are not forced to sell long-term capital gain property for this particular reason. The alternative and more relevant choice, then, is for them either to give the property away or to retain it. In the overwhelming majority of cases, it will cost the taxpayer more to make the gift and save something in taxes than not to make the gift and save nothing in taxes. That is, the individual will be worse off, in the sense that his net wealth will be less, after he makes a charitable gift than he would be if he were to keep his property. This is true even beyond the reduction in net wealth, for by making a gift in the form of securities, real estate, or other income-producing property the taxpayer also gives up the future income that he would enjoy if he kept the property in his possession.

The principal proposal for tax reform in this area is to reduce the amount of the charitable deduction by one-half of the unrealized appreciation on the property. The taxpayer would still have some incentive to make contributions in the form of appreciated property, but instead of taking 100% of the fair market value of the property as a deduction, he would take the fair market value of the property less 50% of the unrealized appreciation as his deduction. One of the provisions in the Tax Reform Act of 1969 made this change with respect to the deduction for gifts of appreciated property to private foundations.[7] While the extension of this rule to gifts of appreciated property to public charities would remove the remote possibility that a taxpayer might "make money by giving it away" (assuming that his only alternative is to sell the property), it would also greatly reduce the incentives

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[6] Since voluntarism is an alternative to reliance on government, charitable gifts may be thought of as a voluntary tax which, like the progressive income tax itself, results in a redistribution of income from the rich to the poor. Most charitable giving directly or indirectly benefits the low and middle income segments of society more than the wealthy. Therefore, by stimulating the wealthy to give more, this provision in the tax law results in a beneficial discrimination in favor of the low-income taxpayers and those whose incomes are so low they pay no taxes at all.

[7] An exception is provided in the case of foundations making qualified distributions of such gifts within a specified time limit.

for making such gifts. A reduction in the incentives for voluntary giving would reduce the flow of individual contributions to educational and charitable recipients, and the loss of contributions income to the voluntary sector would exceed by an astronomical margin any conceivable gain that might accrue from the change as a matter of "equity."

In terms of the public interest, the provisions of the present law have in fact resulted in a flow of charitable and educational gifts in the form of appreciated property that is substantial in amount and important in impact. The testimony on this particular point at the public hearings on tax reform in April, 1973, brought out repeatedly that, for the agencies and organizations in health, education, welfare, and other voluntary fields, these kinds of gifts are particularly vital as a component of total contributions income.

In the case of higher education, it is estimated that gifts of appreciated property account for about one-fourth of total voluntary support from all sources. In 1971-72, for example, roughly $500 million out of the estimated total of $2.02 billion of voluntary support from all sources consisted of gifts of property other than cash. With respect to gifts and bequests from individuals, contributions in the form of property make up about 45% of the total, and more than 60% of the total for gifts of $5,000 or more.[8] Corporate gifts of appreciated property are much less important in the context of total corporate support of higher education, yet they involve tens of millions of dollars worth of assets of significant value to the recipient institutions.

It is clear that the present tax treatment of gifts of appreciated property has resulted in a very considerable tax incentive for charitable giving on the part of those who have such property, and that gifts in this form constitute an important part of the total voluntary support of higher education. The proposed change in the tax law amounts to the imposition of a tax on the donor by reason of his having made the gift. If they wish, taxpayers can avoid this tax by simply not making gifts. It is probable, therefore, that the proposed legislation, if enacted, would very drastically reduce the flow of large gifts in the form of appreciated property. And since the property not contributed is merely retained by the taxpayer, the capital gains would continue to be unrealized.[9]

Under these circumstances, it is difficult to envision how the public interest would be served by the proposal with respect to gifts of appreciated property. There would be little or no increase in tax revenue to the government, yet there would almost certainly be a large decrease in the voluntary support of higher education and other public charities. In view of the increasing financial difficulties of colleges and universities, such a decrease in voluntary support could well make the difference between survival and extinction for some institutions. It would clearly reduce the quality of education at most institutions, public and private alike, or increase the burden of governmental support of higher education, or both.

Charitable Bequests

Under the present estate tax law, there is no ceiling on the amount of a charitable

[8] Julian H. Levi and Sheldon Elliot Steinbach, *Patterns of Giving to Higher Education II*, Washington, D.C., American Council on Education.

[9] Under the present law, such gains may never be taxed as such. For estate tax purposes, the "value at time of death" is normally used for all of a decedent's property, and the tax is based on the gross estate, so valued, less certain deductions.

bequest which may be deducted from the gross value of the estate for tax purposes. One may, therefore, bequeath his entire estate to charitable recipients, in which case the taxable estate would be zero and no estate tax liability would arise. Any part of the estate may be taken as a charitable deduction in arriving at the taxable estate, and the gift may be in the form of either a specific bequest or a residual bequest.

In recent years there has been a significant upsurge in the total amount of charitable bequests. In 1950, for example, they amounted to $274 million; by 1960 they had risen to $951 million, and by 1972 they had reached an estimated level of more than $2.7 billion. The factors accounting for this ten-fold increase include (a) an increase in the number of estates of taxable size, (b) an increase in the total value of estates for which tax returns have been filed, and (c) the fact that charitable bequests have been rising as a percentage of total estates. Much of this reflects the fact that increasing proportions of the population are reaching the senior age groups in a state of economic independence and affluence. In addition, there is the effect of inflation on the value of property vis-a-vis the constant exclusions and deductions in the estate tax law.

This dramatic rise in the total amount of charitable bequests has served to call attention to instances in which wealthy persons bequeath very large fortunes to both private foundations and public charities. The question posed by the tax critics in this area is essentially one of political philosophy, with overtones not of equity but ethics. They feel that no one should have the right to leave as much as 100% of a large estate to a favorite charity, tax free; that every estate in excess of some arbitrary size should provide some income to the public Treasury, regardless of how it is distributed. They propose, therefore, that there should be a limitation on the contributions deduction for estate tax purposes, and that the limitation should be 50% of the adjusted gross estate. The regular rates of tax would apply to the remaining taxable estate even if the entire balance were left to charitable beneficiaries.

Since all estates are ultimately liquidated, it is clear that charitable and educational beneficiaries would bear the full burden of such a change in the estate tax law, even though it is the decedents' estates that actually make the tax payments. The proposal therefore amounts to a recommendation for a tax on charity, since it would have no other effect than to divert some part of the flow of bequests from charitable agencies and organizations to the Treasury.

The impact of such a change on the voluntary support of higher education and other philanthropies would be severe. As indicated above, total annual bequests to charitable beneficiaries are now about $2.7 billion and rising. This source of funds, therefore, accounts for roughly 14% of voluntary giving by individuals to the philanthropic sector of society. As for higher education, bequests account for between one-fourth and one-third of voluntary support by individuals, and the total in recent years has been in excess of $300 million annually.

A very high fraction of the bequests received by colleges and universities is designated for endowment and other capital purposes. The proposed change in the estate tax law, therefore, would not have as large and immediate an impact on operating budgets as would the proposed changes in the income tax law. However, such

a change would have a long-run impact in that it would slow the growth of endowment funds and thus slow the growth of endowment income which is an important part of the operating budget for many of the institutions of higher education.

The total endowments of all colleges and universities amounted to about $15 billion in market value at the end of academic year 1971-72. The annual increase averaged about $500 million in the preceding five years. Bequests, therefore, constitute an important source of the growth of endowment funds. The income from endowment funds is an important part of the operating budgets of most private, and many public, colleges and universities. The growth of endowments, and the accompanying increase of endowment income, is a factor that is essential to the ability of the institutions of higher education to meet the rising costs due to inflation and expanding enrollment. It would be tragic if the law were changed so that this source of endowment principal were significantly restricted; the percentage increase in the annual revenues of the Treasury would be insignificant, while the decrease in the annual flow of voluntary support to the institutions of higher education would be appreciable.

The Minimum Taxable Income Proposal

One source of the interest in tax reform is the widespread belief that there are many loopholes in the present tax law which enable persons with high incomes to escape their "fair share" of total taxes. There are, in fact, many provisions in the Internal Revenue Code which either give preferential treatment to income earned in certain ways or which allow special exclusions and deductions to certain groups of taxpayers. It is, indeed, possible for a person to enjoy a very high income and yet pay little or no income tax on that income.

The provisions in the tax law which make this possible were enacted to achieve various purposes which Congress thought desirable at the time. For example, the percentage depletion allowance granted to the producers of mineral resources was adopted for the express purpose of giving encouragement to the search for and the development of these resources. In other cases, the provisions were thought necessary to correct inequities that had developed with the passage of time. And, as with long-term capital gains, the preferential tax treatment of some kinds of "income" arose from a genuine belief that it is not ordinary income and should not be taxed as such; other examples of unusual types of income would include the "bargain element of a stock option at the time of exercise," and certain income earned outside the United States.

Some taxpayers are able to utilize these and other provisions of the tax law so as to eliminate most or all of their taxable income and thus be liable for little or no tax. The Administration has offered a tax reform proposal designed to prevent this and to insure that most individuals would be forced to pay some minimum amount of income tax, regardless of the sources of that income and regardless of the exclusions and deductions that the taxpayer might legitimately claim.

This "Minimum Taxable Income" proposal (MTI), as it is now structured, would have an important impact on voluntarism because it does not distinguish between charitable contributions and other personal deductions. Instead, charitable

contributions are lumped in with all other personal deductions, such as medical expenses, taxes, interest payments, and casualty losses, and the total of all such deductions would, in effect, be subject to a limitation of 50% of income.[10]

The effect of this proposal, therefore, is to reduce the maximum allowable deduction for charitable contributions below the present 50% of adjusted gross income. The amount of the reduction would vary from case to case, but for numerous taxpayers the allowable deduction for charitable gifts would become zero. In a great many instances, therefore, this proposal would penalize philanthropic giving.

In these circumstances, donors would be discouraged from making any gifts beyond a variable limit. Contributions would be deductible only to the extent of the difference between 50% of income and the total of all other deductions. Consequently, many taxpayers will reduce their giving in order to avoid the implicit tax penalty.

Although the concept of the MTI has many desirable features as an expression of policy, the absence of any special provision for the encouragement of charitable giving is contrary to the long-standing public attitude on this subject. Charitable contributions should not be treated the same as other personal deductions, because they result from voluntary and discretionary decisions on the part of the taxpayer which are not motivated by financial gain, but rather by the desire to help worthy causes which need such help. All other deductions either provide the taxpayer with some tax relief for involuntary costs (e.g. medical expenses and casualty losses) or provide him with a partial offset to some expenses for which he receives a benefit (e.g. local taxes and interest payments on borrowed money).

Philanthropic giving is a form of voluntary tax;[11] it would be consistent with the purpose of the MTI to treat charitable contributions as payments for public purposes in lieu of taxes.

The current MTI proposal would reduce charitable giving in another way. It contains no provision for a carryover of any excess deductions. Large contributions, which under the present law qualify for a five-year carryover for any amounts in excess of the permitted maximum, would be discouraged because any excess would be lost forever as a tax deduction. While large gifts are relatively few in number, they account for a disproportionate share of the voluntary support of higher education. In 1970-71, for example, gifts of $5,000 or more represented only 5% of the number of gift transactions, yet they accounted for 75% of all voluntary support received by the institutions of higher education.[12]

According to Treasury estimates, only about 130,000 out of the 35 million taxpayers who itemize their deductions would be affected by the MTI proposal, and the total contributions of this group of taxpayers is estimated currently at $800 million. The loss in charitable contributions from the MTI rule would, according to the Treasury, be in the neighborhood of $300-500 million, depending on how these taxpayers react to the reduction in their tax incentive.

What the Treasury did not estimate is the impact that this loss in contributions

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10 Under the MTI proposal, this is "expanded adusted gross income," defined as adjusted gross income plus four items of preference income, less personal exemptions and a "low income floor."

11 Government entities are first on the list of eligible recipients in the definition of "charitable contributions." See Section 170(c)(1) of the I.R.C. of 1954, as amended.

12 Levi and Steinbach, pp. 10-11.

would have on charitable beneficiaries. Were it all to fall on higher education, for example, it would represent a decrease of between 15% and 25% in the total of voluntary support. It is hard to believe that this kind of a result could be considered to be in the public interest in any way.

Other Proposals

The preceding discussion dealt with the tax reform proposals that are of the most immediate significance to higher education, both because of their potential impact and because of the serious attention being given to them by the tax-writing committees. Other suggestions have been advanced from time to time which also would have an important impact on the voluntary support of higher education.

One of these is the proposal for a threshold or floor, typically 3% of adjusted gross income, below which no charitable contributions would be deductible. While this is said to represent an effort at tax simplification, it would penalize charitable giving by the majority of taxpayers. In 1970, for example, about 29 million taxpayers out of the 35 million who itemized their deductions were in the income groups in which the average charitable contribution amounted to less than 3% of income. The threshold proposal, therefore, would affect the multitude of small contributions that are so vital to the voluntary sector. While the small gift is less important than the large gift to higher education, the total of voluntary support received as small gifts constitutes a significant share of all support, and the removal of this particular tax incentive would seriously impinge on the effectiveness of college and university fund raising.

Another proposal would impose a tax on the unrealized appreciation of long-term property at the time of death, without making any exception for property bequeathed to charitable institutions. Under this proposal, virtually every estate would be reduced in size by the amount of the tax, so that the amounts available for distribution to all beneficiaries, including educational and charitable institutions, would also be reduced. Such a tax would clearly impose a burden on the taxpayer in planning for charitable bequests in the context of his total estate and his preferred disposition. Since about two-thirds of the value of estates bequeathed to colleges and universities is in the form of property, the indirect impact of such a tax on the voluntary support of higher education could be very significant. Here again, the proposal would effectively reduce voluntary giving without increasing substantially the tax revenue to the Treasury and without affecting in any way the fairness of the tax laws as they apply to different income groups.

Finally, it has been proposed to eliminate the charitable contributions deduction entirely and to substitute in its place a tax credit equal to some arbitrary percentage of the total amount of the taxpayer's gifts. The taxpayer would not deduct his charitable contributions from his income prior to calculating his tax, rather he would calculate his tax without taking his contributions into account and then offset some fraction of his contributions against the amount of the tax due. The recommended percentages for the tax credit have varied from 27% to 50%, and there are several variations on the basic proposal in terms of other personal expenditures that might be included.

The proponents of the tax credit proposal assert that it would enhance tax

equity. It is argued that the present deduction arrangement is unfair because the Treasury "subsidizes" the small contributor less per dollar of gift than the large contributor. This differential "subsidy" arises because the progressive tax rate structure necessarily results in a larger tax "saving" for a gift deduction by a high-income taxpayer than for one by a low-income taxpayer. The tax credit would be more fair, it is said, because this "subsidy" would be equal, per dollar of gift, for all taxpayers.

The argument is faulty in many ways.[13] Among other things, it reflects the view that while it is equitable to tax income according to a progressive rate structure, it is somehow inequitable to untax that income according to the same rate structure when it is voluntarily given by the taxpayer for a philanthropic purpose.

Even if the argument were valid, however, the tax credit proposal is by no means a desirable alternative to the present arrangement. In theory, it would be possible to substitute a tax credit for the charitable deduction and to set the percentage at such a level that the increased contributions of the lower income taxpayers would precisely offset the decreased contributions of the high income taxpayers. While the result would be no change in the total amount of philanthropic giving, there would be a very marked change in the distribution of this total among all the recipient agencies and institutions.

As a practical matter, however, there is no way to determine in advance what the appropriate percentage should be in order to maintain the existing flow of individual contributions. It would inevitably involve trial and error. And since the change in the pattern of philanthropic support is also unpredictable, there is a major risk that the effect of the change would be contrary to the national interest.

Moreover, fund-raising activities would become more complex and less efficient. There would be a decline in the number and importance of large gifts and an increase in the number of small gifts. Charitable solicitation, therefore, would face an increase in the fund-raising cost per dollar of contributions received, thus widening the gap between what the donors give and the donees receive. Such a development would clearly be undesirable.

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[13] A complete discussion of the equity question would be much too lengthy for this paper. A technical memorandum on the subject will be made available by the Council for Financial Aid to Education and provided to the interested reader upon request.

III. The Importance of Voluntarism to Higher Education

Almost all of the proposals for changing the tax laws with respect to the charitable contributions deduction would, if adopted, have the effect of discouraging the voluntary support of higher education. This is especially true for those proposals which are being given any serious consideration. In view of the other financial problems of academia, any diminution of voluntary support could hardly come at a more inopportune time. What higher education needs now is more support, not less.

In the past 25 years, higher education has undergone a marked transformation as a social institution and its influence has become deeper and more widely diffused than ever before. It no longer provides education primarily for the small segment of society able to afford the costs involved, rather it provides educational opportunities of an extraordinarily diverse character to a substantial proportion of the population. It is no longer concerned principally with the traditional programs centered on the liberal arts and the professions, rather it is concerned with the totality of educational needs for a technological society characterized by social and economic mobility. It is no longer a collection of "ivory towers" isolated from the mainstream of American life, rather it is a far-flung enterprise intimately concerned with and involved in human welfare and the social issues of the day. It is no longer simply a community of scholars dedicated to teaching and to expanding the frontiers of knowledge, rather it is an aggregation of centers of learning and scholarship, deeply involved with the nature of man and his relation to his environment. In short, it has become a highly-organized instrument for the achievement of many national goals. In this context, voluntarism has come to have a profound effect on the destiny of both the individual and society.

The Importance of Voluntary Support

The voluntary support of colleges and universities has become much more important than its numerical magnitude would indicate. Private gifts and grants to higher education, which were less than $200 million in the mid-1940's, reached a level in excess of $2 billion in 1971-72. This latter figure represents only 6.8% of the total expenditures (operating and capital) of all colleges and universities combined, yet the function of voluntary support is so unique that it exerts a disproportionate influence on the capacity of higher education to serve society.

For the private colleges and universities, which account for more than 75% of the number of institutions, such support is clearly vital to solvency and survival. These schools traditionally rely on private support to meet a substantial share of their operating budgets and virtually all of their capital requirements. It is thus a source of income basic to the ability of private institutions to be free and independent of political authority, and to provide diversity to the system of higher education.

For the public colleges and universities, voluntary support has been essential to their ability to offer education of high quality. Gifts and grants from private

sources often provide the "vital margin for excellence." Since appropriations from state and local government budgets are necessarily determined in the context of total tax revenue and the entire complex of competing demands for such funds, the allocations to the institutions of higher education tend to be limited to the most essential functions. There is seldom any extra money for the marginal activities and programs that make the difference between mediocrity and superiority in education.[14] Private gifts and grants thus provide the public colleges and universities with additional leeway for experimentation, for going beyond the minimum educational effort, and for providing the additional services whch are being increasingly demanded of all higher education, public and private alike.

In larger terms, voluntary support provides the underpinnings for a diversity in higher education that is vital to the independence of all colleges and universities in carrying out their high purposes. Such independence is indispensable to the preservation and extension of educational quality.

The excellence of higher education in the United States is in large measure due to its exceptional diversity. There are now more than 2,600 colleges and universities, some public, some private. They differ enormously in size and structure, and they offer a broad range of programs oriented toward an extensive array of educational objectives. Some are national institutions, independent in outlook from the part of the country in which they are located; others are local in orientation, closely identified with the people and problems of their particular communities. Their constituencies are as varied as the institutions themselves, some serving primarily the members of a religious denomination, others serving special minority groups, and still others are aimed at serving the needs of a cross-section of the population. Some are highly specialized, organized to serve the particular needs of agriculture, the arts, science and technology, religion, medicine, the law, and even education itself. Others are more generalized, with curricula which span a variety of disciplines.

This diversity among the institutions of higher education is a reflection of the pluralistic society of which they are a part. It has arisen because of the pluralism which has been so important in the evolution of all American institutions, political and economic as well as social. Higher education as it exists today was unplanned. It developed at first through the individual initiative of countless educators and philanthropists who perceived a need for particular kinds of colleges and universities in particular places at particular times, and who gave of themselves and their resources that the institutions might be formed, maintained, and expanded. In the past hundred years, public authorities at all levels of government have also come to perceive and value the benefits which accrue to the nation and to all its subdivisions from the broadest possible base of educated citizenry. In this way the great state universities, land-grant colleges, community colleges, and other public institutions have been added to the higher educational establishment to serve the needs of the growing society. Many of these institutions bear the stamp of voluntarism in

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14 "Legislators do not look with favor on the extras that will make the difference between adequacy and excellence. If public institutions are to strive for exceptional performance, they are forced to look to private funds to lift them above the commonplace or the mediocre. Those public institutions that have achieved greatness have done so with the help and encouragement of private resources and private leadership."

Howard R. Bowen, President, University of Iowa, speaking to businessmen in Dallas, Texas, at a CFAE luncheon meeting, March 7, 1969. (Dr. Bowen is now Chancellor, Claremont University Center, and a Director of CFAE).

addition to their sponsorship by state and local governments. Private financial support has been an important source of income for many of these institutions, and in numerous instances the buildings, grounds, and other physical facilities were donated by interested and concerned individuals.

The voluntary contribution of money, time, and energy was responsible for the founding of higher education in the United States, and voluntarism in all its dimensions has been a key element in its development for more than 300 years.

The Early History of Voluntary Support

During the Colonial period private gifts were the dominant source of funds for higher education. Among the nine colleges founded before the Revolutionary War, only one received any substantial assistance from governmental sources; the other eight were established and maintained almost entirely by philanthropists. The survival and growth of these institutions during the seventeenth and eighteenth centuries was possible only because of a continuous flow of gifts and bequests for operating funds and physical facilities.

During the period from [illegible] 1860, it is estimated that as many as a thousand colleges were organized. Most of these institutons were founded by clergymen and supported by local congregations, and their continuance depended directly on their success in raising money. Despite the efforts of many dedicated individuals and the frequency with which appeals for support were directed to the urban centers in the northern and eastern areas, only a small number of these colleges survived as permanent institutions. While it was voluntary giving at the local level that made this boom in new colleges possible, it was philanthropy in its wider dimension that determined which institutions should be maintained and encouraged to grow.

In the years following the Civil War the flow of voluntary support overshadowed all earlier gifts to higher education. Individual benefactors made single gifts measured in millions of dollars, whereas contributions previously had been reckoned in thousands. Many of the older colleges, including those founded in the Colonial period, were transformed into major universities as a result of large gifts from philanthropically-minded citizens. In perhaps two dozen instances, multi-million dollar gifts were responsible for the establishment of new universities as going concerns; these institutions flourished and grew as a result both of large endowments provided by their founders and of continuing support which was attracted to these new centers of learning. This period also saw the creation and development of many of the state universities and land-grant colleges, most of which received financial support from private citizens as well as from the Congress and the state legislatures.

The Period After 1910

In 1889-90, the U.S. Office of Education began to compile some information pertaining to the income and property of colleges and universities. For 1909-10 and later years, the published data included basic figures on the annual level of private gifts and grants, and with the passage of time this information became more detailed and more comprehensive. Summary data from this source, covering the period from 1909-10 to 1965-66, are shown in Table I.

These figures reveal an extraordinary growth in the overall total of private gifts

Table I

Private Gifts and Grants Received by Colleges and Universities
(millions of dollars)

	1909-10	*1919-20*	*1929-30*	*1939-40*	*1949-50*	*1953-54*	*1957-58*	*1961-62*	*1965-66*
Current Funds:									
Educational and General	3.6	7.6	26.2	40.6	118.7	191.3	325.0	450.8	651.1
Less: Contributed Services[a]				7.9	17.8	25.0	37.4	46.6	60.0*
	3.6	7.6	26.2	32.7	110.9	166.3	287.6	404.2	591.1
Student Aid[b]						16.8	32.8	57.0	86.6
Total current funds	3.6	7.6	26.2	32.7	110.9	183.1	320.4	461.2	677.7
Capital Funds:									
Physical plant funds	8.4	7.9	51.4	22.7	72.6	103.9	157.2	226.5	366.1
Physical plant assets[c]							29.0	49.9	73.0
Endowment funds					62.8	100.1	192.7	230.2	282.2
Student loan funds	11.2	51.5	63.5	36.3	1.5	1.9	3.2	8.5	10.4
Other capital funds					2.5	4.5	7.8	19.8	34.5
Total capital funds	19.6	59.4	114.9	59.0	139.4	210.4	389.9	534.9	766.2
Total gifts and grants	23.2	67.0	141.1	91.7	240.3	393.5	710.3	996.1	1,443.9

[a] Not separately collected until 1931-32.
[b] Not separately collected until 1953-54.
[c] Not separately collected until 1957-58.

* Estimated by Division of Research, CFAE

Source: U.S. Department of Health, Education, and Welfare, Office of Education: *Digest of Educational statistics* (1971 Edition), Table 129, p. 100: Surveys of *Financial Statistics of Institutions of Higher Education* (1957-58 to 1965-66); *Biennial Survey of Education in the United States* (1949-50 to 1955-56).

and grants received by colleges and universities. From $23.2 million in 1909-10, the total of voluntary support of higher education rose to more than $1.4 billion in 1965-66. This increase represents a growth rate of 7.7% per year, on the average.

It is very probable that this rate of growth exceeded that of the period before 1909-10 and that the acceleration in the growth of voluntary support is related to the tax laws and their treatment of private philanthropy.

As indicated in Table I, the rise of voluntary support after 1909-10 was by no means uniform. Between 1909-10 and 1929-30, the average growth rate was 9.4% a year. This was followed by the decade of the Great Depression when private gifts and grants fell by a third. After 1939-40, however, voluntary support resumed its upward course, and for the 26-year period ending 1965-66 the growth rate averaged 11.2% a year. For the entire period, the growth of voluntary support exceeded that of the national economy and that of higher education itself.

The rapid growth of educational philanthropy after 1909-10 coincided with the enactment of the income tax and the adoption of the contributions deduction. The jump in the growth rate following 1939-40 occurred immediately after the upward shift in income tax rates at the onset of World War II. There can be little doubt that these relatively high rates of growth were due in no small part to the effect of tax incentives. In 1964 and 1965 there was a reduction in tax rates, and since then the growth of voluntary support of higher education has slowed appreciably.

Voluntary Support Since 1965-66

The only consistent information on overall educational philanthropy since 1965-66 is that compiled in the annual *Survey of Voluntary Support of Education*.[15] Although these Surveys are less comprehensive than those conducted by the U.S. Office of Education, the participating institutions have consistently accounted for about 85% of the private gifts and grants received by the entire higher educational community. Estimated totals for all colleges and universities are shown in Table II.

It is clear that the growth of voluntary support has been slower in the period since 1965-66 than it was in previous years. For the six years ending 1971-72, the estimated totals show an average annual increase of only 5.8% as compared to the growth rate of 11.2% during the period from 1939-40 to 1965-66. With the exception of 1968-69, the percentage increases in every year since 1965-66 have been smaller than the average growth rate in the prior period.

This decrease in the rate of growth of voluntary support is one of the causes of the financial crisis that has overwhelmed higher education in recent years. Between 1965-66 and 1971-72, college and university expenditures increased at an average rate of 12% per year, which is slightly greater than the rate of increase between 1949-50 and 1965-66. The factors responsible for the earlier growth of institutional expenditures – increasing enrollment and rising costs per student – continued with full force throughout most of this recent period, and in addition the rate of inflation accelerated. Although the growth of expenditures has begun to moderate with the slowing in the rise of enrollment, it remains high by historical standards.

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[15] For 1966-67 and later years, the U.S.O.E. figures are either inconsistent with earlier definitions or narrower in coverage. Since 1967-68, for example, only fragmentary data on capital funds have been compiled.

Table II

Estimated Total Voluntary Support Received by Colleges and Universities

(millions of dollars)

	1965-66	*1966-67*	*1967-68*	*1968-69*	*1969-70*	*1970-71*	*1971-72*
Support Received for Current Operations	675	710	800	870	960	1,050	1,110
Support Received for Capital Purposes*	765	770	800	930	820	810	910
Total Support Received	1,440	1,480	1,600	1,800	1,780	1,860	2,020

* Includes gifts for endowment, whether earmarked or placed there at institutions' discretion.

Source: Council for Financial Aid to Education, *Voluntary Support of Education* (various dates).

The decline in the growth rate of voluntary support in the last six years, therefore, has resulted in a significant decrease in the relative importance of educational philanthropy as a percentage of total institutional expenditures, from 9.5% in 1965-66 to 6.8% in 1971-72. The difference between these two figures implies a "loss" of approximately $800 million of gift income in 1971-72 as compared to what voluntary support would have been had it continued to grow at its earlier rate of increase. This sum is equal to more than $300,000 per institution, a figure that could easily have spelled the difference between a serious deficit and a balanced budget for many small and medium-sized colleges.

In view of the impact of inflation and growing enrollment, this estimated "loss" in voluntary support has an even greater significance. The data shown on Table III indicate clearly the character of this development. Prior to 1949-50, the growth of

Table III

Voluntary Support of Higher Education in Relation to Inflation and Enrollment

	Voluntary Support (millions of current dollars)	*Consumer Price Index (1947-49 = 100)*[a]	*Voluntary Support (millions of 1947-49 dollars)*	*Total Enrollment (thousands)*[b]	*Voluntary Support per Student (1947-49 dollars)*
1909-10	23	38.4	60	355	169
1949-50	240	102.3	235	2,659	88
1965-66	1,440	136.8	1,053	5,526	191
1971-72	2,020	175.9	1,148	8,116	141
Average annual percentage change:					
1909-10 to 1949-50	6.0	2.5	3.5	5.2	−1.6
1949-50 to 1965-66	11.9	1.8	9.8	4.7	5.0
1965-66 to 1971-72	5.8	4.3	1.5	6.6	−4.9

Sources:

[a] U.S. Bureau of the Census, *Historical Statistics of the United States, Colonial Times to 1957*, Washington, D.C., 1960, Series E113, E158, E159, pp. 125-127; *Economic Report of the President*, Washington, D.C., 1973, Table C-44, p. 244; data converted to 1947-49 base by Division of Research, CFAE.

[b] U.S. Department of Health, Education, and Welfare, Office of Education: *Digest of Educational Statistics* (1971 Edition), Table 103, p. 77; *Projections of Educational Statistics* (1972 Edition), Table 6; resident and extension degree-credit enrollment for 1965-66 and 1971-72, extension students excluded for prior years. Non-degree-credit enrollment, which was about 800,000 in 1971-72, is not included.

educational philanthropy had not kept pace with the combination of rising prices and growing enrollment, with the result that support per student, in constant prices, decreased by about 50% in the forty years after 1909-10. Between 1949-50 and 1965-66 the situation was reversed, and real support per student made up all the lost ground and more. Concurrent with the slowing in the growth of voluntary support between 1965-66 and 1971-72, however, there was an acceleration in the rate of inflation and an acceleration in the growth of enrollment. As a result, voluntary support per student, adjusted for inflation, *decreased* nearly 5% per year, on the average, and in 1971-72 reached a level below that of 1909-10.

This development indicates clearly that there is an urgent need for a further encouragement of educational philanthropy, not the kind of discouragement that would result from some of the proposals for the tax reform.

As a result of the decrease in the growth of voluntary support and other sources of income, and the continued upward pressure on costs, many institutions of higher education have encountered budgetary deficits. The academic community as a whole has entered a period of severe financial stress. The character and extent of this financial crisis has been well-documented elsewhere,[16] and need not be repeated here in detail. It should be pointed out, however, that educational expenditures grew at an unprecedented rate throughout the fifties and the sixties, and that this growth was made possible by a favorable combination of political and economic factors and public attitudes. At the same time, the upward push on the costs of higher education reflected factors that were largely beyond the control of the colleges and universities.

All this is now changed. Virtually all the sources of college and university income have encountered resistance to further growth, and some of the factors which have tended to increase the costs of education have now begun to moderate. Colleges and universities themselves have taken many of the necessary steps to improve their management procedures and to economize on their use of the available resources. Much has been done in this area and much yet remains to be done, but there is some chance that the institutions of higher education will be able to maintain a viable degree of financial stability in the years ahead.

Their success in this area, however, will depend directly on the continuation of a favorable climate for voluntary support. In this regard, perhaps the most critical single factor of all is the character of public policy with respect to the tax incentives for philanthropy.

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[16] R. H. Atwell and C. W. Atwell, *Adjustments of the Major National Universities to Budgetary Distress.* (1972).

G. Hudgins, *et al. Peoples Colleges in Trouble* (A Financial Profile of the Nation's State Universities and Land-Grant Colleges), (1970).

W. W. Jellema, *The Red and the Black* (Special Preliminary Report on the Financial Status of Private Institutions of Higher Learning), (1971), and *Redder and Much Redder,* (1971).

Earl F. Cheit, *The New Depression in Higher Education (A Study of Financial Conditions at 41 Colleges and Universities),* Carnegie Commission on Higher Education, (1971), and *The New Depression in Higher Education – Two Years Later,* (1973). In his latter book, Professor Cheit states "that (financial) stability is fragile, for it is the product of unusual cuts in expenditure growth and is based in part on favorable assumptions about external conditions – inflation, enrollments, private support, and public policy at the state and federal levels. Clearly, then, it would not take much to destroy the stability and force the institutions on a downward course again."

IV. The Future of Voluntarism in Higher Education

There do exist some provisions of the Internal Revenue Code that are in need of revision. However, those related to the charitable contributions deduction have already been purged of abuse. Philanthropy needs more, not less, encouragement. The charitable deduction has been a continuing fixture of the tax law for over 55 years; it has withstood the test of changing conditions, through prosperity and depression, through peace and war, and through very substantial changes in the relationship between the individual and society. It has served effectively as an instrument of public policy in channelling voluntary initiative and voluntary funds into a host of socially-desirable philanthropic activities, thus helping to preserve some of the fundamental tenets of American character and political philosophy.

It is a fact, however, that at a time when philanthropic needs are growing the charitable contributions deduction and several related provisions of the tax law have come under attack. All of the tax reform proposals which deal with charitable contributions, although designed to achieve other goals, would have the effect of reducing the incentives for philanthropic giving. If enacted into law, such proposals would be certain to result in a decrease of the voluntary support of higher education and other charitable activities. The cost to society of this result is likely to be much greater than any benefits that might be achieved in other directions.

Potential Consequences of Tax Reform

Americans have long had impulses toward generosity that are independent of any tax considerations; philanthropy was a thriving institution before the income and estate taxes came into being. However, the encouragement to voluntary action in the public good which arose from the adoption of the present tax structure has resulted in an upward shift in the levels of giving, and the effects of this change are now built into the economic structure of higher education and other voluntary sectors. The predictable downward shift in giving habits that would result from reduced tax incentives for philanthropy will inevitably do violence to the fragile solvency of all charitable institutions. The probable magnitude of this effect, under present conditions, is likely to destroy much of the cherished pluralism in American life.

Higher education, in particular, will suffer many undesirable changes. At a minimum, there will be a retrenchment of educational programs and other services at many colleges and universities. Among other things, this will involve significant reductions in educational opportunity for substantial numbers of young people who have only recently begun to have any real hope of obtaining a college education. It will also involve some decrease in the quality of education available to those who can continue to attend college. In the extreme, the loss of voluntary support could lead to widespread insolvency among the private institutions of higher education, with all the resultant dislocations of students, faculties, and institutional resources. The losses to society implicit in such developments are incalculable.

Substitution of Government Support Unlikely and Undesirable

It is often argued that any reduction in institutional income as a result of decreased private giving could be replaced by additional governmental appropriations, either through existing programs or through entirely new legislation. Such a development is possible, but it would require significant changes in public policy that are unlikely in the context of national priorities and undesirable in the climate of opinion that continues to favor a pluralistic society. Moreover, since many of the private institutions of higher education are church-controlled, the constitutional principle of separation of church and state, as embodied in the First Amendment, would bar any general appropriations to these colleges and universities from governmental sources.

Even if there should be a willingness to substitute Treasury funds for private funds in the financial structure of higher education, there is an important allocation question. The distribution of funds to the institutions of higher education by public authority is typically on a formula basis, and such formulae are inevitably arbitrary and rigid. By contrast, the allocation of voluntary support is determined by the decisions of many individual and corporate donors who determine their own allocations on the basis of perceived needs and opportunities.

The recipients and the purposes of private gifts and grants are thus determined by millions of private decisions, each of which reflects the preferences of the individual giver as to the uses to which his money should be put. Such preferences, molded in the light of individual knowledge of particular educational institutions and educational priorities, constitute a rich composite of the value standards of an important segment of the population. The sum of many private decisions with respect to the distribution of resources to higher education is inherently preferable, in a free society, to the rigid allocations dictated by any formulae, just as in a free economy the sum of the market decisions of producers and consumers is preferable to the arbitrary dictates of any centralized authority.

Aside from these considerations, the substitution of additional government support for any part of the existing private support is undesirable by reason of the potentially adverse impact on the character and quality of higher education. Any increase above the present 50% share of total governmental funding in the income structure of the institutions of higher education[17] implies that public authority would become dominant in the direction of educational effort. The concentration of the financial support of higher education in government hands necessarily leads to the concentration of influence and control in educational matters, and such authority would all too easily be dictated by political and other non-educational considerations.

Any rise in the importance of governmental funds would weaken the values which are today inherent in the diversity of college and university funding. In due course, there would be a decline in the freedom and independence of educational institutions to determine their own policies and programs. The communities of

[17] The income structure of all institutions of higher education combined has been relatively stable in recent years. General appropriations, support for research and other programs, and student-aid funds provided by Federal, state, and local governments constitute roughly 50% of the total. Income earned by colleges and universities for themselves from tuition, fees, room and board payments, and the revenues of academic departments and enterprises account for about 40%. Private gifts and grants and the income from endowment investments make up the remaining 10%.

interests that now direct the activities of colleges and universities would necessarily become subservient to the monolithic interests of governmental bureaucracy. Uniformity would replace diversity in educational programs and institutional services, rigidity would replace flexibility in educational policy, and the latitude for innovation and experimentation in educational matters would be severely constricted. Colleges and universities would become less responsive to the interests of their students, their supporters, and their communities.

Ultimately there would be an erosion of the capacity of higher education to maintain and extend its contributions to American society. Economic and social progress would be jeopardized, and the vital dynamics of American political life would be seriously impaired. Much of the strength of the United States as a leader in world affairs might well suffer as a direct consequence of this eventuality.

The achievements of higher education in contributing to the welfare of American society have been made possible in large part by the voluntary initiative of countless individuals who have given their time, their talent, and their money to support the colleges of their choice. It is imperative that voluntary support should continue to be encouraged by public policy, and that the provisions of the Internal Revenue Code which provide tax incentives for such support should be maintained and strengthened.

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R127-6M-11-73